



HEDGE CLIPPERS

#HEDGE PAPERS NO. 24 – PUERTO RICO HEDGE FUND VULTURE HOLDOUTS

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PUERTO RICO



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**LOS TIRANOS, LOS VAMPIROS, Y EL TERMINATOR
(THE TYRANTS, THE VAMPIRES, AND THE
TERMINATOR)**

The Puerto Rican debt crisis has recently reached a new stage in negotiations between the government and its bondholders: deals have been reached with many creditors and ad hoc groups have fallen apart, but several creditors are continuing to hold out, intending to squeeze massive profits out of a Puerto Rico on the brink.

Unsurprisingly, this holdout group is led by hedge funds, and unyielding billionaire hedge fund managers.

Sources close to the negotiations have named three of the vulture holdouts: Aurelius Capital Management, Brigade Capital Management, and Monarch Alternative Capital.

None of the three hedge funds is particularly well known – they mostly toil in the arcane, under-scrutinized world of distressed debt, in which “vulture funds” use heavy-handed legal and bargaining tactics to extract maximum profit from failing companies and debt-ridden economies.

They aren’t household names, but they ought to be – the effects of their business practices are felt far and wide in the US and beyond.

Meet Los Tiranos (the tyrants), Los Vampiros (the vampires), and El Terminator.

This report is based on our information regarding the current state of play in the Puerto Rico debt crisis — it will be updated if and when new information is available.

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LOS TIRANOS (THE TYRANTS): *MONARCH ALTERNATIVE CAPITAL*

Despite a relatively low profile, the \$5 billion hedge fund Monarch Alternative Capital has a history of playing the tyrant in debt negotiations, holding out longer than other creditors to win the biggest possible payout at the expense of the people on the other ends of their deals – workers, retirees, taxpayers. ^[1]



Monarch founders Andrew Herenstein and Michael Weinstock are grizzled veterans of hard-core, knock-down, drag-out negotiations.



With a winner-take-all perspective and a take-no-prisoners attitude, they're the tyrants in these talks — and they don't seem to care what or who they harm in the process.

In 2012, for instance, Monarch Alternative emerged as a key creditor in the Hostess Brands failure.^[2]

Monarch was one of two hedge funds that controlled hundreds of millions of dollars in Hostess debt and essentially owned the company in its final months (other investors had been wiped out).

The hedge funds demanded steep pay and benefit cuts, and only one of the Hostess unions conceded – the other went out on strike.

According to *Business Insider*, “without large union concessions—what some would say, total union capitulation—the hedge funds decided Hostess would have to die.”^[3]



The company announced that it was dissolving not long after, and 18,500 workers were laid off.^[4] The federal government ended up taking on pension obligations. It is unclear how much Monarch Alternative made on the deal.

In Puerto Rico, Monarch Alternative may have the right connections to push an agenda that again punishes people in order to extract profit.

One of the key negotiators in Puerto Rico on behalf of the US Treasury is Antonio Weiss, who was a colleague of Monarch Alternative founders Andrew Herenstein and Michael Weinstock at Lazard during the 1990s.^[5]



Herenstein and Weinstock have continued their relationship with Lazard, retaining the firm as a placement agent during a 2014 fundraising round while Weiss was still there.^[6]

The hedge fund is also ramping up campaign contributions to politicians with influence over how Puerto Rico's crisis will be handled by the federal government.



Just three weeks before presidential candidate and Florida Senator Marco Rubio went to the island and announced his opposition to legislation that would provide bankruptcy relief, Herenstein and his wife reportedly co-hosted a fundraiser for Rubio in the Hamptons.[7] Herenstein had already donated \$2,700 to Rubio in May.[8]

Herenstein's fundraiser for Rubio — followed by Rubio's newly outspoken position against bankruptcy protections — is a perfect example of how hedge fund billionaires use campaign cash to control politicians and manipulate public policy across America – including in Puerto Rico.

Herenstein and his wife have also donated \$10,600 to presidential candidate Ted Cruz,[9] who recently co-sponsored a failed immigration bill, with Rubio, that would have imposed penalties such as prison time for undocumented immigrants.[10]

Herenstein's wife, Terri, also donated \$100,000 to B-PAC, a hedge fund backed PAC that supported ultra-conservative Senate candidates in 2014, including Iowa Senator Joni Ernst, who has said she opposes a federal minimum wage,[11] wants to abolish the IRS and the EPA,[12] and recently introduced a bill to defund Planned Parenthood.[13]



LOS VAMPIROS (THE VAMPIRES): *BRIGADE CAPITAL MANAGEMENT*

Of the three hedge funds, Brigade Capital Management is by far the largest, with close to \$20 billion in assets under management.

Brigade Capital is not focused solely on distressed debt in the way that the other two funds are, though it has often been a key player in other high-profile debt deals.

More than the other two holdouts, the hedge fund managers at Brigade Capital are the vampires of the bunch, relying heavily on investments from public pension funds even as their debt plays target the public purse.^[14]

Brigade Capital's clients include major public pension funds in New York State and New York City, Massachusetts, Rhode Island, Pennsylvania, Ohio, Maryland, and other states.^[15]

At the same time that Brigade Capital relies on public funds, it has been aggressive in its pursuit of debt payouts that impose steep costs on taxpayers.

In Jefferson County, Alabama, for instance, a Brigade Capital principal led negotiations on behalf of hedge fund holdouts that reportedly won a 33% return on the county's debt.^[16]

While the hedge funds profited, Jefferson County taxpayers were stuck with higher sewer rates, the county's hospital for the poor cut back operations, and many county workers were laid off.^[17] (Monarch Alternative was also among the holdouts in Jefferson County.)

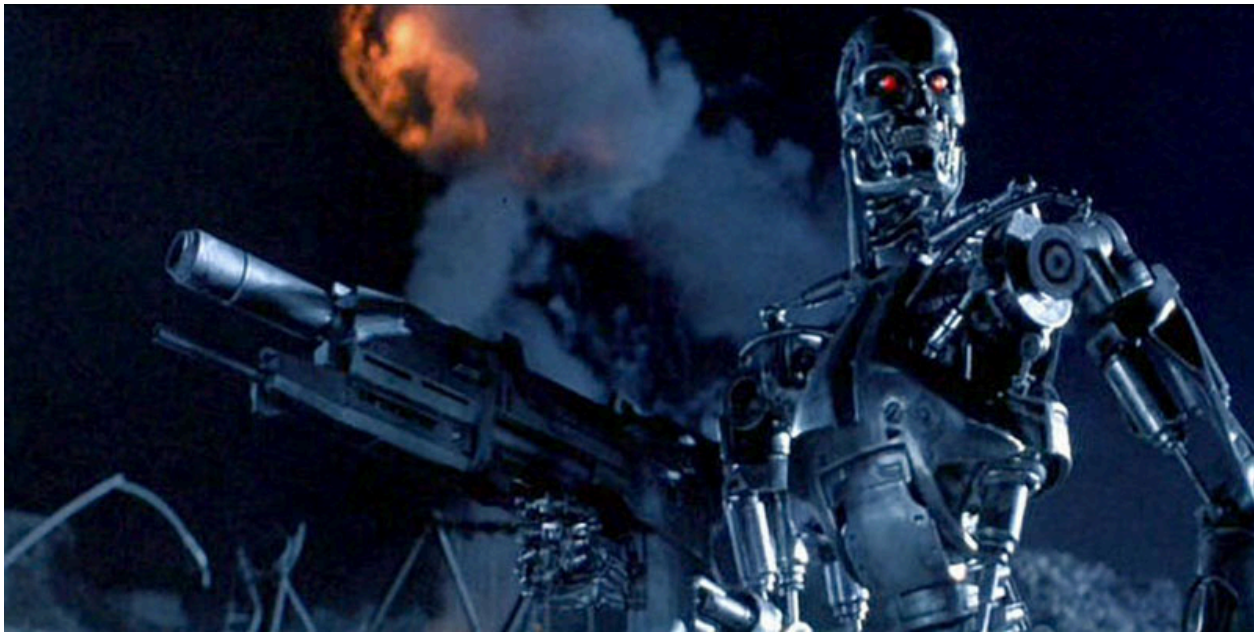


Brigade Capital is also willing to invest heavily in manipulating democratic processes and elections when its business is threatened. It is a major investor in and creditor to casinos, and in California spent nearly \$4 million opposing a referendum that would have threatened one of its casinos by allowing a rival casino to open.^[18]



EL TERMINATOR: AURELIUS CAPITAL MANAGEMENT – MARK BRODSKY

Aurelius Capital Management, a \$5 billion fund, is run by Mark Brodsky, a former bankruptcy lawyer so persistently litigious in his drive to extract profits from bankrupt companies and indebted countries that he has come to be known as “The Terminator.”



That moniker may be too generous, since some Terminators play the hero.

A defining moment in Brodsky's career came in 2004, when he made headlines for architecting a debt litigation strategy targeting companies that had gone bankrupt due to asbestos litigation exposure. [19]



Elliott Management, where Brodsky worked at the time, bought up the companies' debt for pennies on the dollar and then found ways to litigate its way to bigger payouts –by challenging the asbestos victims' share.

At one point, as part of a sophisticated public relations and lobbying strategy, Brodsky took to the pages of the *Wall Street Journal* to argue that asbestos victims had too much power in the bankruptcy process. [20]

He won the recusal of a judge in that case, and launched his own fund on the strength of that victory the next year.

Since striking out on his own, Brodsky has been a high-profile holdout in many debt cases.



Most notably, he has partnered with his former boss, Paul Singer, in Argentina, where the two hedge fund managers bought up debt for pennies on the dollar following the country's default and have litigated their way to a potential 1,600% profit. [21] Brodsky has claimed that his fund will make \$500 million in profit on the deal. [22]

While Brodsky was at Elliott Management, the fund was involved in similar vulture trades in Peru and Congo-Brazzaville.[23] It bought debt for pennies on the dollar and litigated their way to massive payouts from countries with high levels of poverty.[24]

More recently, Aurelius has been on the scene looking for higher payouts in bankruptcy cases including Tribune Companies, Anglo Irish Bank, and Energy Future Holdings, and has also been on the scene in Detroit and Greece. [25]

He goes to great lengths to secure profits in bankruptcy proceedings – in the Washington Mutual bankruptcy case, a judge said that Aurelius and other funds may have profited from insider trading.[26]

Brodsky recently purchased a \$53 million unit at One57, a new luxury building in Manhattan with a lucrative tax deal that shields residents from millions in taxes.[27] Brodsky apparently reinvests part of his fortune in politicians that tend to favor low taxes on wealthy hedge fund managers like him – he is a major donor to the National Republican Senatorial Committee (\$15,000), the RNC (\$40,000), and Mitt Romney (\$5,000).[28]



[1] See Delphi bankruptcy, which resulted in a profitable deal for hedge funds at the expense of taxpayers, retirees, and workers: <http://www.thenation.com/article/mitt-romneys-bailout-bonanza/>; Hostess bankruptcy, below, which resulted in layoffs and pension payment cutoffs; and other deals, such as Jefferson County – <http://www.reuters.com/article/2013/05/08/us-usa-detroit-funds-idUSBRE94704P20130508> – and Detroit – <http://archive.freep.com/article/20140714/NEWS01/307140094/Detroit-bankruptcy-hedge-funds>

[2] <http://fortune.com/2012/07/26/hostess-is-bankrupt-again/>

[3] http://www.businessinsider.com/how-hostess-failed-hedge-funds-v-unions-2012-11?pundits_only=0&get_all_comments=1&no_reply_filter=1#comment-50a7b90969beddaa6b000022

[4] <http://www.cnbc.com/id/49852161/>

[5] <http://www.monarchlp.com/team/founders/michael-a-weinstock/>, <http://www.monarchlp.com/team/founders/andrew-j-herenstein/>, and <http://www.wsj.com/articles/SB123655956839366515>

[6] <https://www.pehub.com/2013/12/monarch-alternative-seeks-850-mln-for-third-fund/>

[7] <http://jewishinsider.com/3819/2016-comes-to-the-hamptons-this-weekend/>

[8] <http://www.opensecrets.org/indivs/search.php?name=herenstein&cycle=All&sort=R&state=&zip=&employ=&cand=rubio&submit=Submit>

[9] <http://www.opensecrets.org/indivs/search.php?name=herenstein&cycle=All&sort=R&state=&zip=&employ=&cand=cruz&submit=Submit>

[10] <http://www.bloomberg.com/politics/articles/2015-10-20/senate-blocks-immigration-crackdown-bill-backed-by-ted-cruz-marco-rubio>

[11] <http://www.thegazette.com/subject/news/government/fact-check/fact-check-joni-ernsts-minimum-wage-stance-20140628>

[12] http://www.iptv.org/iowapress/story.cfm/story/11721/ip_20140424_4131_ernst_cutting_spending

[13] <https://www.yahoo.com/health/the-female-face-behind-the-senates-bill-to-defund-125752372087.html>

[14] See Jefferson County and Puerto Rico.

[15] Prequin: Brigade Capital Management.

- [16] <http://www.bloomberg.com/news/articles/2013-06-04/jefferson-county-reaches-deal-with-creditors-on-bankruptcy-exit> ; <http://www.wsj.com/articles/SB10001424052702304868404579191874090087990>
- [17] <http://www.wsj.com/articles/SB10001424052702304337404579212553163071992>
- [18] <http://www.sacbee.com/news/politics-government/election/article3026510.html>
- [19] <http://www.euromoney.com/Article/1001988/Elliott-Associates-aggression-captures-low-risk-returns.html?single=true> and <http://www.wsj.com/articles/SB110410617152209675>
- [20] <http://www.wsj.com/articles/SB110410617152209675>
- [21] <https://www.washingtonpost.com/news/worldviews/wp/2014/06/26/three-things-to-know-about-the-supreme-courts-ruling-on-argentine-debt-and-why-it-matters-to-argentina-and-the-world/>
- [22] <http://www.washingtonpost.com/news/business/wp/2014/07/31/meet-the-billionaire-hedge-fund-manager-who-pulled-argentina-into-default/>
- [23] <http://www.washingtonpost.com/news/business/wp/2014/07/31/meet-the-billionaire-hedge-fund-manager-who-pulled-argentina-into-default/>
- [24] <http://blogs.wsj.com/moneybeat/2014/06/25/what-happens-when-the-the-vulture-funds-start-circling/>
- [25] Detroit: <http://www.freep.com/story/news/local/detroit-bankruptcy/2014/10/21/hedge-funds-detroit-bankruptcy-fgic/17670251/>; Greece: <http://www.cnbc.com/2015/02/19/what-tragedy-hedge-funds-look-to-score-on-greek-recovery.html>; AIB: <http://www.wsj.com/articles/SB10001424052748703727804576011821714853378>; Energy Future Holdings: <http://www.wsj.com/articles/SB10001424052748703409304576167253478066590>; Tribune: <http://www.reuters.com/article/2015/08/19/tribune-aurelius-idUSL1N10U15920150819>
- [26] <http://dealbook.nytimes.com/2011/09/14/judge-says-hedge-funds-may-have-used-inside-information/>
- [27] <https://hedgeclippers.org/1464797090949/one57/>
- [28] <http://www.opensecrets.org/indivs/search.php?name=brodsky&cycle=All&sort=R&state=&zip=&employ=aurelius&cand=&submit=Submit>